

CORONAVIRUS

Unsanitized: Why Banks Don't Want to Help Small Businesses

Also, beware the middleman. This is The COVID-19 Daily Report for April 3, 2020.



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Masrur Odinaev/CreativeCommons

First Response

The small business lending program from last week's survival aid package, known officially as the Paycheck Protection Program (PPP), started this morning. In true "got the book report in under the wire" format, the Small Business Administration issued an

“interim final rule” for the program last night. The rule asks for comments and *also* goes immediately into effect, and these are emergency times with speed of the essence, so I’ll allow it.

The rule intends to cut off **growing unrest from lenders** leading up to the PPP launch, threatening quick relief for millions of small businesses in the form of forgivable loans meant to maintain payroll. Smaller banks wanted a higher interest rate to make the program more lucrative; SBA **doubled the interest rate** from 0.5 percent to 1 percent. Bigger banks wanted effective immunity from prosecution for fraud in handing out the loans; the rule states that lenders “will be held harmless for borrowers’ failure to comply with program criteria.” The lender doesn’t need to verify any documentation or underwrite in any way, though they still must comply with the Bank Secrecy Act and file any suspicious activity reports. Banks get significant processing fees: 5 percent on loans up to \$350,000, 3 percent on loans larger than that up to \$2 million, and 1 percent on loans between \$2 million and \$10 million, the limit of the program. It’s like an hour’s work for a junior banker to process these loans and the bank can get between \$10,000 and \$100,000. And the fully guaranteed loans can be sold directly into the secondary market, so banks don’t have to wait to recoup. It’s about as free as money gets.

None of these rules are unexpected; banks had been **screaming about liability** but the statute said plainly they would be held harmless. Yet JPMorgan said it **would not be ready** to accept applications today, and thousands of others are balking at compliance with the Bank Secrecy Act, just basic anti-money laundering rules. Even Bank of America, which did **launch its web portal** for accepting applications at 9am ET this morning, has restricted help to “Small Business clients with a business lending and a business deposit relationship at Bank of America.” Now, the *Prospect* is a small business. We have one bank for our deposits and another bank we have used on occasion for lending. BofA, the first lender in the program, will only help businesses that have both. Plenty of businesses operate on a cash basis and don’t do any borrowing. They’d too be out of luck.

So why the reticence from the banking sector? I think liability is a red herring; are they really afraid of the heavy regulatory hand of Steve Mnuchin (or any law enforcer involved in the financial crisis)? It looks to me like they don’t want to do the work. Every expectation is for an **absolute crush** of applications. Thirty million small businesses could be on the line here. The compliance requirements are minimal but banks always whine about the expense of that; that’s why BofA is restricting to already-vetted customers. And the guidelines, which have been **“changing by the minute,”** could change again. So why bother with the hassle? The money’s good, but it’s marginal, and the big banks think in billions, not millions.

I've been extremely concerned that this could be HAMP 2.0, though there are key differences. HAMP, the government loan modification program, was run through *predatory* banks who delighted in using the program to turn a profit, crushing homeowners in the process and foreclosing on them anyway. PPP, the government small business rescue, is being run by *disinterested* lenders, who don't see enough upside for them to make this a priority. This is risk-free money (5 percent in this environment!) and the banks aren't very into taking it.

Maybe they will be cajoled, but again, the operative word is speed. I've talked to dozens of small business owners who are confused by this program and also **desperate to participate**. There's not going to be enough money—Congress gave \$350 billion—to begin with. If lenders are slow to open the spigot, a lot of these businesses will go down. They don't have any cash reserves. There's a lot of concern. Maybe SBA should have found someone more willing to act quickly. Like themselves.

Vital Stats – An Update

I have some changes to announce in this section. Since Unsanitized began, I've been posting statistics of U.S. confirmed cases, deaths, and completed tests, along with more recently hospitalization data. You can find that at **New York Times, Johns Hopkins University**, the **COVID-19 Tracker**, this **hospitalization tracker**, and elsewhere.

But I've grown disillusioned with the reliability of really any country's figures. You may have heard the term from computer science "garbage in garbage out." If the data is bad then what it tells you when you feed it through any system is also bad. I've despaired that we **won't know the true death toll**, that it's based on what countries count as a COVID-19 death, or how many tests they're doing and on what kinds of patients, or even if the tests are reliable (it seems **they aren't**). I can't stand behind these numbers, so I'm not going to print them anymore. If we get more reliable figures, maybe I'll alter my decision. I think we can say at this moment: things are bad, even if we don't know exactly how bad.

Stuck in the Middle With You

The tragedy of a chaotic supply chain, with cities and states and hospitals and the federal government all competing with each other over the same small supply of masks and gowns and ventilators, has been **well-documented**. One thing that comes through in the reporting is **the role of the middlemen**.

There have always been middlemen in hospital supplying: monopoly middlemen known as group purchasing organizations that control purchases of ordinary supplies (like masks and gowns and generic drugs) for nearly all hospitals. They have been getting a **direct airbridge of supplies from abroad**, courtesy the federal government, to flow out to their customers. The problem is that FEMA, in this case, is competing with cities and states and bidding up prices, and supplies are so short that everyone's going outside these middleman contracts and looking for *other* middlemen to find them supply. So the monopoly GPOs have proven ineffective, as the monopoly is on the other side of the supply chain, at the point of manufacture.

These **pop-up middlemen** are pure grifters, it seems. People are forming on-the-spot businesses for medical supply distribution. They are somehow finding storehouses of product and brokering deals at huge markups; New York, ground zero for the crisis, is paying up to 15-fold markups. Everyone's out for themselves: the separate governments, the hospital buyers, the producers, the middlemen. And with desperation and a chaotic supply, that breeds corruption and gouging.

We're about to see middlemen elsewhere, too. With the news that Americans could wait up to five months for the \$1,200 direct payments authorized in the CARES Act, there's no doubt that "direct payment advance" merchants will arrive on the scene. For a fee, they'll advance you your check and take it once you get it. It'll be a short-term, high-interest, guaranteed loan. We see this with tax refunds all the time (they're called refund anticipation loans, and **H&R Block** makes a lot of money off them).

When capitalism breaks down and desperation sets in, the middlemen come out, promising relief. This just siphons resources away from where they're intended: hospitals get fewer supplies, struggling individuals get less money. Middlemen are not service providers but avatars of a broken system. Government can play a role in fixing that, taking over supply chains in times of crisis and building systems to speed immediate individual relief. But they don't, and so we have the middlemen.

Today I Learned

- **701,000 drop in payrolls** in March, and that only really captures the middle of the month. The worst stat: 61,000 jobs lost in health care. (CNBC)
- This "**select oversight committee**" on the bailouts sounds good but would have to actually be authorized by a House resolution, and nobody's in Washington. This is a shadow play. (Politico)
- Amazon **smears an employee** they fired for organizing a walkout. (Vice)

- The Democratic National Convention has been **postponed to August**. (*New York Times*)
 - The scam of **pandemic bonds**. (Jacobin)
 - It would be better if there wasn't a **buildup of corporate debt** that's now getting downgraded. (*Wall Street Journal*)
 - A **\$75,000 bill** for COVID-19 treatment for uninsured Americans. (CNBC)
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